Improve the Economic Vitality of Businesses and Individuals
Tollgate #2

1. Map of Causal Factors (Separate Document)

2. Assess the performance progress in this result area-Update (New information since Tollgate #1 only)

3. Propose high-level purchase strategies for this result area. What are the key areas where the state should take action, and how (if known at this point)?

We have identified ten strategies that follow from the strategy map. The highest priority strategies include:

- Strategy 1: Develop Markets by Promoting of Washington Products and Services.
- Strategy 2: Increase productivity/quality by promoting Innovation
- Strategy 4: Reduce Costs Through Flexible Regulatory Methods
- Strategy 10: Improve the effectiveness of all economic development investment through improved Coordination

SUCCESSFUL BUSINESSES

Strategy 1: Develop Markets by Promoting of Washington Products and Services.

This high-level strategy is one of the Economic Vitality Team's highest priorities. It includes the following activities:

- Addressing trade and regulatory barriers that prevent access to foreign markets for Washington products;
- Conducting trade missions to promote Washington products via government-to-government negotiations;
- Promoting collective selling for groups of Washington businesses;
- Retaining and growing Washington companies;
- Promoting of investment in Washington by foreign and out-of-state companies (recruitment).
- Marketing the state to promote tourism and support retention and recruitment efforts.

These activities not only improve the prosperity of businesses by improving their sales, but also help to diversify Washington's economy and reduce the impact of business cycles by bringing in money from outside Washington's economy.

A well-rounded economic development program requires efforts to retain existing companies, promote growth and expansion of existing companies, create new companies, and recruit businesses and investment from out-of-state.

Retention and growth of existing firms is absolutely critical. According to data developed and analyzed by the Department of Employment Security, employment growth of existing companies clearly exceeds employment growth due to relocations. Yet recruitment also plays an important role to replace the economic activity of companies that will inevitably leave the state or go out of business.

A marketing program can support all of these efforts. But marketing cannot be effective if programs that encourage companies to invest and grow are not in place.

Washington currently spends relatively little money on marketing, recruitment of new businesses, or retention and growth of existing businesses. Local economic development partners see marketing as a function that must be led by the state.

There are several important opportunities on the horizon that make these strategies important right now. With respect to international trade, the most important opportunities involve the expansion of the middle class in third-world markets such as China and India. By familiarizing these countries with Washington products, we can begin to develop loyal customers among those members of the middle class. Additional investment in overseas representatives in these areas may pay dividends for years to come. The Beijing 2008 Olympics also offer opportunities for Washington's design and construction industries to work in China. We must also take advantage of several important tourism opportunities such as the Lewis and Clark Bicentennial and the Vancouver 2010 Olympics.

Strategy 2: Increase productivity/quality by promoting Innovation

This strategy is one of the four highest priorities for our group. This high-level strategy includes the following:

- Increase R&D
- Improve technology transfer
- Support entrepreneurship
- Provide technical assistance
- Provide access to capital

Research and Development adds value to existing products and services. It also can lead to new products and services that can create entirely new markets. Improving technology transfer increases the private and public benefits of research. Entrepreneurship is required to ensure that ideas are tested in the market. Ideas that find both technical and market success can generate new companies that may grow to provide additional diversification and strength to the economy. Technical assistance can improve the success of entrepreneurs, and access to capital ensures that they have the funding they need to grow.

Table 1 shows the continuum of interventions required to build an innovation economy. Each of these stages must be successful to derive the maximum economic benefit from investments in innovation. State government does not play the primary role in most of these areas. For example, while R&D is primarily funded by the federal government and by corporations, state government provides funding for faculty and some of the scientific infrastructure necessary for universities to obtain these federal grants. Similarly, business assistance is provided by a wide variety of federal and nonprofit organizations; the state can play a role in coordination. A single point of contact for all types of business assistance available in the state could be a very valuable tool for entrepreneurs, particularly if it the content is controlled and verified.

Technical assistance to companies for product development is often viewed as something that should be funded by state government, but it is not clear where the greatest return for those investments might be. Access to capital is primarily a private-sector issue, but the state can play a supporting role by ensuring that Washington companies are ready to present their case to funders.

The programs listed in the table are generic terms for existing federal and state programs. Those in bold indicate programs for which state funds are currently spent. The State of Washington has traditionally spent very little in this area, beyond the capacity building investments provided for our research universities. One area where significant R&D investments have been made by the state is in agriculture, where R&D keeps new crops in the pipeline to maintain productivity and to address changing environmental conditions in which crops are grown in Washington. It also provides new products for niche markets and produced jobs through value added and exports.

An important consideration in the development of strategies to promote innovation is the strategies' ability to **address other outcomes** that are important to Washington's citizens. For example, innovation in energy and environmental technologies can assist in creating a new industry and creating new markets for Washington companies, but it can also help us achieve our environmental goals. Innovations in health care and information technology may be able to reduce the cost of improving the health of Washington citizens. IT innovations can also improve the efficiency of government.

Being strategic about the innovation economy requires that we have an understanding of the structural changes technology will create. We must bring education, workforce training, regulation, and infrastructure investment in line with technological change to ensure that we maximize its benefits and minimize the costs of structural adjustments. For example, technological advancement often causes changes in the skills required in a particular industry. We must ensure that those losing jobs as technology advances have a chance to enjoy technology's benefits through retraining. This requires that we monitor these changes so that we can respond.

Table 1. Interventions to Build an Innovation Economy

Product Stage/ Type of Intervention	Build Research Capacity	Company Basic/Applied Research	Design for Manufacturing	Product Launch	Enhance Product	Product Maturity
Technical Assistance	**Centers of Excellence**		Advanced Manufacturing Centers		**MEP (USDOC)** Sea Grant (NOAA) CREES (USDA)	
Business Assistance		**Incubators, Business Development**; Science Parks				
Funding	EPSCOR (NSF) Federal Funding	ATP **SBIR** **STTR** **State Research Grants**	State - Sponsored Seed Funds		SBA Loans	

Strategy 3: Diversify the Economy to reduce the impact of business cycles

By focusing our efforts on a variety of sectors that bring in money from outside the state, we reduce the impact of business cycles, particularly those that are driven by local industry dominance (e.g. aerospace).

This type of industrial policy is controversial. Some claim that we cannot “predict winners”—choose the industries that are most likely to provide economic benefits. However, given the limited resources available for economic development, Washington has chosen to focus its efforts on specific industries. CTED has been working over the last few years to narrow down the focus industries. Other agencies, such as the Workforce Training and Education Coordinating Board, Employment Security, and the State Board for Technical and community colleges, have also adopted a cluster strategy in their grant activities.

As these industries are identified, they should be based on the following factors:

- Current strength of the industry;
- Growth and investment potential;
- Potential to leverage trade opportunities;
- Their ability to help us accomplish other objectives (e.g., clean energy or environmental technology industries).

Reducing Costs

Strategy 4: Reduce Costs Through Flexible Regulatory Methods

This strategy is one of the four highest priorities for our group.

Flexible regulatory methods can take many forms, but we discussed the need for two types of strategies in this area:

- Reducing the paperwork and bureaucracy associated with meeting requirements by using technology to increase the coordination and consistency between agency requirements and processes;
- Where feasible, providing performance based standards rather than mandating specific methods for compliance.

The first strategy reduces costs for companies because delays cost money.

The second reduces costs because it allows a company to identify the least cost method for meeting standards for environmental and consumer protection. This accomplishes several of our goals: it can reduce costs for business, promote innovation, and ensure that an environmental or safety standard is met, rather than simply proscribing a technology.

Experiments in performance-based standards have shown promising results[1]. Our team feels that this is an area with great opportunity. We hope a pilot project for a specific environmental performance area can be developed.

Strategy 5: Reduce costs and improve the effectiveness of other economic development efforts by investing in strategic infrastructure

Investment in strategic infrastructure supports some of the other strategies, such as company recruitment and R&D. Companies looking to expand or relocate often look for specific types of infrastructure. Furthermore, basic infrastructure is necessary to promote healthy communities (see below).

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[1] Snyder, Lori D. 2003. "Are Management-Based Regulations Effective?: Evidence from State Pollution Prevention Programs." Regulatory Policy Program Working Paper RPP-2003-21, Cambridge, MA: Center for Business and Government, John F. Kennedy School of Government, Harvard University. http://www.ksg.harvard.edu/cbg/research/rpp/RPP-2003-21.pdf

Water storage is a critical issue for future job growth and retention. The lack of adequate water storage forces us to choose between water for fish and water for communities and farms. Additional water storage can reduce the need for these kinds of trade offs. We suggest that additional work on water storage be explored.

Strategy 6: Reduce costs by ensuring Washington's tax system supports competitiveness.

In its tax policy, Washington State must balance two competitiveness issues – the need for an adequate and stable tax structure to fund essential services and the need for a competitive tax structure that does add extraordinarily to the cost of doing business in this state. As the globalization of business continues to take place, there is an increased need for uniformity, simplicity, and the harmonization of tax systems to enable businesses to comply with tax reporting requirements easily and inexpensively.

Washington may have an opportunity to reduce costs for business by harmonizing its tax system with other states. Companies tell us that the idiosyncrasies of our tax system increases their tax compliance costs.

VIBRANT COMMUNITIES

Strategy 7: Improve communities by making housing more affordable.

Strategies for expanding affordable housing can improve the vibrancy of communities and the prosperity of individuals. For larger metropolitan areas, the jobs-housing balance plays an important role in the livability of a community. Higher density, well-designed housing with amenities in urban growth areas provides attractive, affordable, and accessible housing to a variety of income levels. Well-designed compact communities allow people to avoid long commutes, which can reduce congestion, and therefore, cost of building roads. In smaller, more rural communities, it is often hard for low-income individuals to find affordable housing that is close to services that they need, particularly if they do not own a car.

Nationwide, housing is becoming less affordable especially for low income individuals. Rent as a percentage of household income has increased from 19% in 1960 to 26% in 2000. For households in the lowest quintile of the income distribution, rent as a percentage of income has increased from 47% in 1960 to 55% in 2000.

Market demand, not land constraints, is the primary determinant of housing prices[2]. However, there is
also evidence to show that land use regulations can increase the cost of housing [3]. One of the key questions in this debate is whether the land use laws that increase housing costs also serve to decrease the costs of infrastructure. There is evidence that well-crafted

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[2]"The Link Between Growth Management and Housing Affordability: The Academic Evidence", Arthur C. Nelson, The Brookings Institute, February 2002.
[3] Quigley and Raphael, Journal of Economic Perspectives, Winter 2004.

growth management policies that remove regulatory barriers, especially the exclusionary effects of low-density-only zoning, can improve the supply of affordable housing. Adequate public facilities ordinances can raise density and thereby encourage more affordable types of housing[4]. If this is the case, we could make an argument for providing some kind of public support for middle-income housing that supports land-use goals.

The opportunity lies in identifying areas with a jobs/housing imbalance and analyzing whether improving that balance will take people off the road. The challenge is in finding a way to support affordable housing goals without violating the constitution. Under current law, the state can provide infrastructure that supports affordable housing but can only subsidize housing for low-income people.

Strategy 8: Fund Basic Community Infrastructure

As noted earlier, strategic infrastructure can be important for attracting new businesses and supporting expanding businesses. In some cases, local economic development efforts are thwarted by a lack of basic infrastructure capacity. Thus, investments in expansion of basic infrastructure can help to create jobs.

The Infrastructure Coalition estimated a funding gap of over $3 billion dollars in 2002. This gap represents the difference between the cost of implementing the capital plans in local governments' growth management plans and the revenue available to pay for the infrastructure. This gap has likely grown since 2002. Although CERB has received some additional funding, some of that was simply a shift of resources from one infrastructure account (Public Works Trust Fund) to another.

One area of opportunity for improvement right now is in the crisis for health care access in rural communities. Efforts to attract new businesses to rural areas are often thwarted by a lack of health care access. This strategy is primarily the responsibility of the Heath Care results team; however, there is an obvious tie here to economic vitality.

Strategy 9: Support Community Involvement, Planning, and Leadership

When community members are trained in the processes that support vibrant communities (planning and grant writing, etc.) and provide leadership to help get others involved, they can provide great leverage for state and local funding.

The Small Communities Initiative provides evidence of the impact that a small amount of coaching and capacity building can accomplish for a community. We recommend that this program be examined to determine the factors that have made it successful, and to see whether its replication and expansion can further leverage state and local funds.

[4] Nelson, 2002.

Strategy 10: Improve the effectiveness of all economic development investment through improved coordination

Many of these strategies are dependent on others. A coordinated investment strategy can ensure that we receive the greatest benefit from each investment. For example, a coordinated program for recruitment/retention, infrastructure, flexible regulation, and workforce training may provide a very attractive package and improve the effectiveness of recruitment and retention. If it is also focused on one of the traded sectors mentioned above, the benefits of that investment for the economy are maximized.

Another example is the coordination of R&D, technology transfer, entrepreneurship, technical assistance, and access to capital. Although state government does not generally take the lead role in **all** of these issues, they all must be available to maximize the returns to the economy from investment in R&D. The state's role, then, is to ensure that the conditions exist for each of these steps to take place. In some cases, that means the state provides direct financial and technical support. In others, it means the state merely sets the rules and ensures a fair and competitive environment.

We recommend that cross-agency teams be developed to address issues related to specific projects, industries or sectors. This accomplishes both the coordination function and the objective of providing a single face of government to the public.

4. Provide guidance to agencies for budgets, analysis and legislation

A. Identify operational or legal barriers to the implementation of the high-level strategies.

Recruitment and retention strategies are hampered by the prohibitions against lending of the state's credit. For example, the Legislature has made some attempts to assist the asparagus industry by providing processing equipment to the industry. However, the department of Agriculture is struggling to find a legal way to do that.

Flexible regulation may be deterred by the difficulty of verifying compliance with performance standards. This may not be a problem for all kinds of environmental standards. However, for some, specific advances in monitoring technology may be needed to verify compliance, and this may be expensive.

The state's role in providing affordable housing is also limited because currently state statute only allows the state to fund housing for low income people.

B. Identify opportunities to reduce the price or improve the efficiency of current services.

The coordination of infrastructure programs may provide an opportunity to reduce the cost of making grants and loans for infrastructure. Currently, there are several groups that provide infrastructure for community and economic development: the Public works Board, the CERB board, Department of Ecology, and DOT.

During the 2002 POG discussion, we discussed the idea of a "foundation" type of structure where requests for grant funding for the state would come through a single process. This proposal did not get far, but it may be time to reconsider whether this is an opportunity to use our infrastructure funds more strategically.

We also suggest searching for ways to use technology to reduce the duplication of information that must be provided to different state and local agencies by the same business or individual. This approach—to develop shared information systems where data required are very similar—may save money for both the agencies (costs can be shared among the agencies needing the information) and the businesses. One example of this is the Master Business License application.

C. Identify new initiatives and areas of budget focus that should be pursued based on Tollgate #1 and #2 analysis.

A "Quicksites" program to coordinate investments in planning, infrastructure, and workforce training for specific industries in local areas as they identify their industry clusters. This could be structured as a grant program that combines some existing resources (e.g. CERB and workforce training grants) with some new resources that can provide assistance with strategic, environmental, and land-use planning.

An entrepreneurship program that coordinates the efforts of existing organizations providing technical and business services for entrepreneurs;

A pilot program for **performance-based regulation**;

Design an **initiative for supporting innovation in energy, environmental, and health care** that create jobs while contributing to other important POG outcomes.

D. Identify specific research projects and budget proposals that may aid the team's development of the detailed purchase plan in the fall.

Inventory technical and other assistance for entrepreneurship, identify holes and where the state can play a major role in integrating services, making them seamless.

At what stage do most firms fail and why? Is there a role for the state in helping them get through that stage?

What environmental programs might lend themselves to a performance rather than technology-based standard? How much money would this save companies regarding compliance? Would it stimulate innovation?

How effective is technology transfer at the research institutions compared with other institutions across the nation? Are there steps that can be taken to improve it?

In what regions is the shortage of affordable housing affecting the performance of the economy? Where is the jobs/housing balance most out of balance? What kinds of regulatory changes or infrastructure investments can address the balance?